

LAW OFFICES

STRANG, FLETCHER, CARRIGER, WALKER, HODGE, & SMITH, PLLC

CARLOS C. SMITH
WILLIAM C. CARRIGER
RICHARD T. HUDSON
EWING STRANG
LARRY L. CASH *
CHRISTINE MABE SCOTT *
J. ROBIN ROGERS # *
G. MICHAEL LUHOWIAK
GREGORY D. WILLETT
MARK W. SMITH *
STEPHEN D. BARHAM

OF COUNSEL
ROBERT KIRK WALKER
FREDERICK L. HITCHCOCK

400 KRYSTAL BUILDING
ONE UNION SQUARE
CHATTANOOGA, TENNESSEE 37402-2514
TELEPHONE 423-265-2000
FACSIMILE 423-756-5861

October 6, 2003

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S. BARTOW STRANG
1882-1954
JOHN S. FLETCHER
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JOHN S. CARRIGER
1902-1989
JOHN S. FLETCHER, JR.
1911-1974
ALBERT L. HODGE
1910-1997
F. THORNTON STRANG
1920-1999

* ALSO LICENSED IN GEORGIA
* ALSO LICENSED IN ALABAMA

The Honorable Deborah Taylor Tate
Chairman
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243-0505

Re: Docket No. 03-00072
Electric Power Board of Chattanooga

Dear Chairman Tate:

We are enclosing an original and thirteen copies of the Internal Audit of the Electric Power Board of Chattanooga's compliance with TRA Telecommunication requirements. We are also enclosing an original and thirteen copies of the Internal Audit of the Electric Power Board of Chattanooga's compliance with TRA Telecommunications Code of Conduct.

Please contact us if you have any questions or need any additional information or documentation.

Sincerely yours,



William C. Carriger
For the Firm

WCC:tm
EPB/TEL - #204
Enclosures

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memo

P.O. Box 182255

536 Market Street

Chattanooga, TN

37422

www.epb.net



To: Harold DePriest

CC: Larry Hinds
Preston Suggs

From: Internal Audit *JA*

Date: October 3, 2003

Subject: Audit of EPB Compliance with TRA Telecommunications Requirements

Executive Summary

Purpose

An audit of EPB Compliance with TRA (Tennessee Regulatory Authority) Telecommunications requirements for fiscal year 2003 has been completed. The objective of the audit was to determine if EPB is in compliance with the conditions set forth in TRA Docket No. 97-07488 and any supplemental conditions or provisions ordered by the TRA. The code of conduct was not reviewed in this audit, but was reviewed in a separate audit.

Scope

The results of the audit are based on a review of TRA Docket No. 97-07488, a review of procedures, audit tests deemed necessary under the circumstances, and inquiries and observations made by Internal Audit.

Opinion

In our opinion, EPB is in compliance with the conditions set forth in TRA Docket No. 97-07488 and any supplemental conditions or provisions ordered by the TRA, except for minor exceptions. Minor exceptions in certain areas should be corrected.

DETAILS OF OBSERVATIONS AND RECOMMENDATIONS

Introduction – How to Read This Report

Each of the audit observations listed in this section of the report contains five specific elements or parts.

1. Criterion – The standard used by the Auditor in evaluating the matter being audited. It may be a Board policy, a law, a regulation, a contractual obligation, or a generally accepted accounting or business practice.
2. Condition – What the Auditor found to exist in the course of the audit.
3. Cause – The reason for a deviation from the standard.
4. Effect – The result or risk caused by a condition deviating from the standard.
5. Recommendation – The Auditor's statement of actions that could be taken to correct the deficiency noted.

INDEX TO OBSERVATIONS

1. EPB is in compliance with TRA Docket No. 97-07488, except for minor exceptions.
2. Minor exceptions require correction.

Distribution for response:

Observation 2 sent to:

Gary Hurst for a response
Copy to: Preston Suggs; Larry Hinds

1. Observation:

EPB is in compliance with TRA Docket No. 97-07488, except for minor exceptions.

Criteria:

The TRA Docket No. 97-07488 sets forth requirements for EPB to properly separate Telecommunications from electric power accounting data, provide assurance that subsidization does not occur, and to properly allocate cost.

Condition:

EPB is in compliance with major provisions of TRA Docket No. 97-07488. Some examples of compliance with major provisions include:

- a. Telecommunications accounting transactions are distinguishable from electric accounting transactions.
- b. Cost assignment and allocation are based upon the proscribed principles of: directly assignable costs; directly attributable costs; indirectly attributable costs; unattributable costs; intercompany loans; and taxes.
- c. Services provided to an affiliate pursuant to a tariff filed with a regulatory authority are recorded in the appropriate revenue accounts at the tariffed rate.
- d. Telecommunications maintains a bank account separate from those of the electric system for deposit of revenues.
- e. Leases between the Electric System and the Telecommunications System are at the highest rate paid by other outside parties.
- f. Telecommunications service revenues are recorded directly to Telecommunications revenue accounts as they are earned.
- g. Telecommunications issues Reporting Requirements to the TRA on an annual basis.

Cause:

Management has made efforts to diligently comply with TRA requirements.

Effect:

Overall, EPB is in compliance with TRA Docket No. 97-07488, except for minor exceptions.

Recommendation:

N/A

2. Observation:

Minor exceptions require correction.

Criteria:

The TRA Docket No. 97-07488 sets forth requirements for EPB to properly separate Telecommunications from electric power accounting data, provide assurance that subsidization does not occur, and to properly allocate cost.

Condition:

Minor exceptions were noted:

- a. Depreciation rates for furniture different between Telecommunications and Electric.
- b. Mapping System costs were not allocated to Telecommunications.
- c. The fiber in the telecommunications wire and cable plant accounts should possibly be in the telecommunications capital lease plant accounts. However, this could not be determined because there is not a written agreement regarding the fiber.
- d. Some telecommunications fiber plant units were not transferred from the electric plant ledger.
- e. Leasehold Improvements are charged to Telecommunications, but may also be included in the building rental being charged. However, this could not be determined because there is not a written agreement. Also, without a written agreement, it is not possible to determine if depreciation for leasehold improvements should be accelerated due to the planned move to a new downtown office building.
- f. The general allocator was calculated using operating expenses. The TRA agreement specifies the use of "expenses" for the calculation, but does not define expenses.
- g. The tariff schedule has not been updated to reflect new services/products now offered.

Cause:

Minor oversights were made in interpretations, information gathering, and calculations. Also, the changing environment and growth of Telecommunications requires process improvements to be made periodically.

Effect:

Minor improvements could be made in compliance with the TRA agreement.

Recommendation:

The minor exceptions noted above should be reviewed and corrected.

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P.O. Box 182255
536 Market Street
Chattanooga, TN
37422
www.epb.net



To: Harold DePriest

CC: Larry Hinds
Preston Suggs

From: Internal Audit *JA*

Date: October 3, 2003

Subject: Audit of EPB Compliance with TRA Telecommunications Code of Conduct

Executive Summary

Purpose

An audit of EPB compliance with the TRA (Tennessee Regulatory Authority) Code of Conduct for fiscal year 2003 has been completed. The objective of the audit was to determine if EPB is in compliance with the Code of Conduct as stated in TRA Docket No. 97-07488.

Scope

The results of the audit are based on a review of the Code of Conduct section of TRA Docket No. 97-07488, review of procedures, and inquiries and observations made by Internal Audit.

Opinion

In our opinion, EPB is in compliance with the Code of Conduct conditions set forth in TRA Docket No. 97-07488. Minor improvements should be made in certain areas to further ensure compliance.

DETAILS OF OBSERVATIONS AND RECOMMENDATIONS

Introduction – How to Read This Report

Each of the audit observations listed in this section of the report contains five specific elements or parts.

1. Criterion – The standard used by the Auditor in evaluating the matter being audited. It may be a Board policy, a law, a regulation, a contractual obligation, or a generally accepted accounting or business practice.
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INDEX TO OBSERVATIONS

1. EPB is in compliance with the Code of Conduct section of TRA Docket No. 97-07488.
2. Minor improvements should be made in certain areas to further ensure compliance.

Distribution for response:

Observation 2 sent to:

Larry Hinds, Preston Suggs for a response.

1. Observation:

EPB is in compliance with the Code of Conduct section of TRA Docket No. 97-07488.

Criteria:

The Tennessee Regulatory Authority (TRA) Docket No. 97-07488 sets forth a Code of Conduct guiding the relationships between the Electric System and the Telecommunications System.

Condition:

EPB is in compliance with the Code of Conduct provisions of TRA Docket No. 97-07488. Examples of areas of compliance include:

- a. The Electric System does not allow advertising or promotional materials to be inserted in the monthly billing statements.
- b. The Real Yellow Pages phone book lists separate phone numbers for the Telecommunications System (648-1500) and the Electric System (756-2706 and 648-1372).
- c. There is no indication in advertising, promotional materials, or sales efforts, that consumers who purchase products or services from Telecommunications will receive preferential treatment by the Electric System.
- d. There are no indications that employees of the Electric System specify a preference for any product or service of the Telecommunications System over like services from a third party provider.
- e. There are no indications of joint marketing of Telecommunications and Electric System services.
- f. Telecommunications does not obtain credit under any arrangement that would permit a creditor, upon default, to have recourse to the assets of the Electric System.
- g. There are no indications that EPB discriminates between Telecommunications and any other entity in the provision or procurement of goods, services, and information, or in the establishment of standards.

Cause:

Management has made efforts to diligently comply with the Code of Conduct requirements as set forth in the TRA Docket No. 97-07488.

Effect:

EPB is in compliance with the Code of Conduct provisions of TRA Docket No. 97-07488.

Recommendation: N/A

2. Observation:

Minor improvements should be made in certain areas to further ensure compliance.

Criteria:

The Tennessee Regulatory Authority (TRA) Docket No. 97-07488 sets forth a Code of Conduct guiding the relationships between the Electric System and the Telecommunications System.

Condition:

Minor improvements which could further ensure compliance were noted:

- a. One Telecommunications employee, a former Electric System employee, had computer access to customer information obtained by the Electric System. There are no indications he actually accessed any information.
- b. The approved policy on Intra-Company Interactions has not been placed on the Intranet.
- c. The telecommunications service agreement signed by customers does not specifically authorize release of EPB electric system customer credit data.
- d. Customer credit checks are being completed for Telecommunications without receiving a signed copy of the Telecommunications service agreement.

Cause:

These minor improvements had not been previously considered.

Effect:

Telecommunications employees could access electric system information. Published policies placed on the Intranet would make them easily available to employees to help them better understand the requirements in business relationships between the electric and telecommunications systems. Specific authorization of release of EPB electric system customer credit data attached to all requests for credit checks would further ensure compliance.

Recommendation:

The minor improvements noted above should be considered.